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ABSTRACT

Following an explanation of the Eureka Project, which studies the financing of higher education opportunities in California, introductory information is provided on the effects of student financial aid in California on both students and colleges. Some points to be considered in understanding the relationship between student aid and institutional finance include the magnitude of student aid in the budgets of colleges and universities; the impact of financial aid on a college's ability to fulfill its enrollment targets; the effects of different kinds of aid on institutions; the uniformity of the effects of student aid across all segments of higher education; institutional expanding or contracting as a result of changes in the flow of aid; institutional responses to the challenges of managing student aid; and the role student aid plays in furthering the missions of many colleges and universities in California. Financial aid falls into the categories of aid from government and private outside sources, aid from the institution from gifts and endowment funds, and aid from institutional general funds. Information is provided on: trends in student financial aid by segment; student financial aid programs and their impacts on institutional finance; and the role of student financial aid in institutional finance (by segment). The segment in which the connection between student aid and institutional finance seems most direct is in the independent sector. Tables, charts, and graphs are included. (SM)

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THE EUREKA PROJECT

A Review of Student Financial Aid in California

Maintaining Balances:

The Relationship Between Student Financial Aid and Institutional Finance

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Arthur S. Marmaduke
Former Director
California Student Aid Commission

CONSULTANTS
Frederick Biedenweg
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Eugene Cota-Robles
Assistant Vice President
University of California

Deborah Daniels
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William Van Dusen
Principal Consultant, Brookdale
Associates and Former Staff Director,
National Task Force
on Student Aid Problems

Timothy Warner
Associate Provost
Stanford University

Barbara Wolfinger
Consultant in Public Opinion Research

Raymond E. Wolfinger
Professor of Political Science
University of California, Berkeley

THE EUREKA PROJECT

A Review of Student Financial Aid in California

Maintaining Balances:

The Relationship Between Student Financial Aid and Institutional Finance

March 1988

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PREFACE

Student financial aid has become a major and complex educational industry. This year in California alone expenditures will be approximately $1.5 billion in all forms of financial assistance—grants, loans, and jobs. It is not only large, it is also complex. Anyone who has been associated with student financial aid is soon struck by how complicated the rules and structure are and how the students and colleges must deal with a multitude of agencies and organizations.

Thirty years ago student financial aid in California was less than $10 million. The few government programs that existed were relatively simple in design. While funds were inadequate, the standards and procedures were comprehensible to all involved. Administration was, by today's standards, simple. Limited student financial aid, largely scholarships, was an activity funded by individuals, college endowments, and local groups.

Over the last three decades all financial aid has grown as governments have become major players and the composition and sources of aid have markedly changed. In the last ten years loans have replaced grants and scholarships as the principal form of student aid. With a massive infusion of loan funds through commercial lenders, the nature of student financial aid has changed.

As student financial aid has assumed a larger role in postsecondary education, it has become more important to review the policies that have undergirded it. Policies, either as specifically adopted or developed in an evolutionary way, need to be reviewed for their past effect, current value, and future utility. Problem policies need to be identified and policies appropriate for the balance of this century developed.

Concerns about student aid policies led to the creation of The Eureka Project, a privately organized, funded, and directed review of student aid policies in California. It is entirely funded by major grants from the James G. Irvine, Weingart, and Haynes Foundations, and by a supplemental grant from the Atlantic Richfield Foundation.

The Eureka Project is under the general direction of a board of directors, with more technical and specific advice to the project given by a steering committee composed of representatives of interested groups and institutions in California. A staff of consultants has come together to direct and write the various studies under The Eureka Project.

The Eureka Project is studying the financing of higher education opportunities in California and the impact of current financial aid programs upon the formal structure of higher education and students. There is concern that the door of educational opportunity may be closing, that the health and vitality of quality independent institutions could be at risk, and that the current student financial aid system has a wide range of unintended consequences.

The Eureka Project anticipates issuing approximately a dozen reports. These reports will endeavor to stimulate policy review of student financial aid and

financing of higher education in California and will be offered by the Board of Directors as thoughtful documents for that purpose. The reports will not necessarily represent the views of members of the Board of Directors or of the four California foundations whose grants have made The Eureka Project possible.

This particular report is the work of Timothy R. Warner, Director of University Budgets and Associate Provost at Stanford University, and Frederick M. Biedenweg, Assistant Vice President for Information Resources at Stanford.

A number of individuals have contributed to this report in a variety of ways. Of course, they bear no responsibility for this published version. We are especially grateful to Raymond F. Bacchetti of Stanford for his encouragement and continued support of the project, and for his critical reading of the early versions. In addition, Marge Dickinson of UC Davis, Robert Huff of Stanford, Larry Litten of the Consortium on Financing Higher Education, and Arthur Hauptman gave very helpful guidance.

A number of administrators from the sample of independent institutions that were part of this study provided essential information and important insights on the relationship of student aid to the finances of their institutions. We note particularly Veronica Tincher of USC, Israel Rodriguez of Pepperdine, John Pfaffinger of Loyola Marymount, George Giacomini of Santa Clára, Edward Crocker of Mills, George Tenopir of Whittier, Dean Buchanan of Cal Lutheran, David Winter of Westmont, Thomas Hixon of California Baptist, William Richardson of Dominican, and Sandee Blechman of the San Francisco Art Institute. In addition, discussions with Kate Jeffery and Larry Hirschman of the University of California, Donald Ryan of San Jose State, and Glenn Smith of the San Mateo Community College District were particularly useful in understanding financial aid in the public sector institutions.

Special assistance in providing, analyzing, and preparing data came from: Dana Shelley of Stanford University, Roxanne Reeves, Hans Giesecke of the Association of Independent California Colleges and Universities, and Don Hills of the California Student Aid Commission.

It is hoped that the studies from The Eureka Project will be useful references for individuals who will be deciding the future of student financial aid in California.

Arthur S. Marmaduke
Executive Director
The Eureka Project

EXECUTIVE SUMMARY

Current research on student financial aid has tended to focus on the impact of aid on students. There has been far less work on the impact of aid on the educational institutions themselves. But, as any college president or institutional budget officer will testify, student financial aid plays a major role in the finances of colleges and universities. This paper attempts to shed some light on that relationship by looking in an impressionistic and descriptive manner at the role student aid plays in the finances of California's public, independent, and proprietary institutions.

The paper begins with a review of the trends in government student aid over the past decade. Three very important changes have occurred:

- Growth in government aid in the proprietary sector has increased markedly. That sector is now receiving more federal student aid—in all forms—than any of the other segments of postsecondary education in California. In terms of total government aid (state and federal) the proprietary segment has grown at an 18.8% annual rate and is now second to independent colleges in total government aid received.
- There has been a clear shift in the kind of financial aid students are receiving. In 1975-76 loans accounted for about a quarter of the aid students received, while scholarships and grants comprised about two-thirds of aid. By 1985-86, however, the total aid pie was cut very differently with loans and grants comprising equal shares of aid, each with about 46%.
- In the decade of the 1980s, total government funded student financial aid has declined or remained constant in real terms in all segments of California postsecondary education, except for the proprietary institutions. The independent colleges and the community colleges experienced the largest such declines. The concern is that independent colleges, particularly the smaller colleges, can no longer maintain a commitment to both socio-economic diversity and to quality education.

Having reviewed the trends, the paper then looks at some of the important factors that define the relationship between student financial aid and institutional finance, with the amount of aid and the level of control exercised by the institution the most important. And, it is not surprising that there is more aid and greater institutional control of aid in the independent sector than elsewhere in California postsecondary education. The paper goes on to review in depth the relationship between student financial aid and the principal government aid programs.

The final chapter provides a comparative analysis of the impact of aid on institutional finance by segment. Of significant interest here is the effect of changes in sources of aid over the past decade on the institutional financial structure. The most significant impacts occurred in the independent sector

which, because of its higher prices, relies more heavily on aid than any of the other segments. As state and federal grant funds were reduced in the late 70s and early 80s, financial aid provided directly by the independent colleges themselves grew dramatically. This strong and sustained commitment to aid appears to have come by increasing tuition and by sacrificing other mainline academic priorities. Many institutions participating in the study, particularly those without significant endowments, have now reached the point where their strong commitments to aid can no longer continue. There are too many other institutional priorities in need of attention.

The result of reductions in institutional aid will be a further widening of the net price differential between public and independent colleges, a decrease in diversity of the student bodies of independent colleges, and a potential drop in enrollment. Ironically, any excess capacity so created comes at a time when the University of California is being pressed to expand enrollment.

INTRODUCTION

When most people think of the effects of student financial aid, they think, quite naturally, of the effects on students. And in fact, most student aid effectiveness studies do focus on students—as well they probably should. But the impression that may be left in the mind of the casual observer is that somehow the educational institutions themselves don't have much of a stake in the business of student financial aid.

It's almost as if the college or university has been portrayed as a sort of "black box" in the whole process. The student goes in, a little financial aid is added to provide the necessary oil for a smooth transition and to insure continuing progress, and, at the end of four or more years, a graduate emerges. So, while there's been considerable discussion about the effects of aid on students, there have been few Mr. Goodwrenches of student financial aid who can reveal the mysteries of the student aid "oil" and its effects on California's colleges and universities.

That's unfortunate because student aid has an important effect on institutions—indeed a vital one. Understanding the relationship between student aid and institutional finance requires that some important questions be asked, such as:

- What is the magnitude of student aid in the budgets of colleges and universities? How much is provided by the institution, by governments, and by private sources?
- What is the impact of financial aid on a college's ability to fulfill its enrollment targets?
- Do different kinds of aid have different effects on institutions?
- Are the effects of student aid uniform across all the segments of higher education?
- Have changes in the flow of aid, particularly from government sources, caused any particular parts of an institution to expand or contract?
- How have institutions responded to the challenges of managing student aid and to the perceived need to lobby for the preservation and expansion of student financial aid?
- What role should student aid be playing in furthering the missions of the many colleges and universities across the state?

While it will be difficult to address each of these issues thoroughly, this paper will attempt to look in a descriptive and impressionistic manner at the relationship between student financial aid and the "black box" of institutional finance. Exploring the issues arising from that relationship should help to reveal that students aren't the only ones with a stake in financial aid policy. There are effects on institutions, as well.

The relationship between institutional finance and student aid certainly isn't new. In the early 19th century many Eastern colleges, notably Harvard and

Yale, attempted to change their image as wealthy schools by offering scholarships. They suddenly found themselves having to budget for student aid and to take into account the effects of aid on other parts of the college. In 1827, for example, Princeton reduced its tuition—surely the ultimate form of student aid—in order to attract a broader spectrum of students. The linkage between this form of financial aid and other key expenditure items was not lost on the Princeton administration as it subsequently reduced faculty salaries to offset the loss of tuition revenue. (Frederick Rudolph, *The American College and University,* Vintage, p.189)

Since World War II the growth of government student aid programs in their multitude of forms and sources has played a fundamental role in the financing of higher education. Its importance has not been lost on college presidents, causing David Stockman to comment that the presidents "may say they care about students but what they really care about is financing their budgets."* While they certainly care about both, Stockman was right in identifying the fact that student financial aid has an impact on the budgets of colleges and universities. In many independent institutions, for example, as much as 60% of the tuition revenue is received in the form of student aid, much of which comes through established government grant or loan programs.

It has long been the case that the price colleges and universities charge students is less than the cost of education. In public institutions the difference can be quite substantial and is covered principally by funds allocated from the state. Independent institutions, not having access to direct payments from the state, rely on other sources, such as gifts and endowments. Regardless of the tuition levels and regardless of the difference between cost and price, some students simply find the tuition levels prohibitive. To provide more students with access to higher education and to give them some measure of choice among institutions, various forms of financial aid have been created.

From the institutional standpoint these forms of financial aid fall into three categories:

1. financial aid from outside sources, both government and private;

2. financial aid from the institution from gift and endowment funds restricted to that purpose; and

3. financial aid from institutional general funds.

The first of these categories is important to the institution because it is, in effect, general revenue as it goes to pay for tuition, fees, room and board.

The second is important because it is money, typically income from endowment and current gifts, that the institution has no choice but to spend on financial aid. If the demand for financial aid was not there, the institution would be forced to let this money sit in reserves, much to the distress of the donors who have provided it. Restricted aid is also important because when it grows faster than institutional prices it will offset general funds used for student aid.

The third is critical because these are funds over which the institution has control and, for one reason or another, has declared necessary to provide further discounts in the price charged to certain students. Although accounting rules require these funds to show in the institution's financial statements as an expense, they are, in effect, a price discount to students. For that reason they probably ought to be viewed as income foregone.

While student aid brings the opportunity of college to the students who might not otherwise attend, it also brings students to those colleges that are under-enrolled—or which seek particular kinds of students (e.g. minority students). Although some may frown at his apparent cynicism, Chester Finn, Assistant Secretary of Education, makes a sobering point when he writes: "Though student aid is most often discussed in the high minded language of equal opportunity, from the viewpoint of institutions whose well being depends on having enough students it plays a more utilitarian role, not very different from the discounts, rebates, and bargain days encountered in the commercial world." (Chester E. Finn, Jr., *Scholars, Dollars and Bureaucrats.* Washington: Brookings, p.59)

Any study of the relationship between student aid and institutional finance must, then, acknowledge the importance of price and, in particular, the price differential between the public and independent sectors. In California, where the public sector dominates and where fees are among the lowest in the country, this is particularly important. The tuition/fee differential is now about 80 to 1 between the independent sector and the community colleges; 11 to 1 between the independent sector and the California State University; and 5.5 to 1 between the independent sector and the University of California.

*Thanks to Professor Michael McPherson, Williams College, for unearthing this quotation.

Clearly, these price differentials have implications for student financial aid. And indeed, one of the original purposes of the California State Scholarship Program, the precursor to the Cal Grant Program A, was to provide a price subsidy to the best students in the State, thus allowing them the choice, not only among public institutions but, if they so desired, of an independent college.

Such large price differentials between public and private education raise the question of relative magnitudes of student financial aid among the segments and form the starting point for this study. How much aid are we talking about in California? What are the forms of that aid? To which segments of higher education is it going and in what amounts? In essence, we need to look at the trends—to understand the flows of aid over the past decade or so. Consequently, an analysis of the trends will be the subject of the first section of this paper.

In looking at these trends it will come as no surprise that in each segment of higher education in California there are a wide variety of student financial aid programs provided by the state and federal governments, by institutions, and by private donors. And each may have a different impact on the financial structure of that particular segment. But because government programs are so dominant and because changes in them may have major impacts on the finances of colleges and universities, the second piece of our analysis will be to review the principal government aid programs and their impacts on institutional finance across the various segments.

As important a role as the state and federal governments have played in student aid programs, it has surely not been a consistent one. Changes in government aid policies have put pressure on institutions over time. The ebbs and flows of federal and state funding for student financial aid have impacts on many parts of an institution's financial structure. In particular, the changes we've seen in government student aid over the past decade raise a number of interesting questions, such as:

- Does a drop in government student financial aid mean the institution should pick up the difference out of its own funds, thereby leaving the student in a neutral position? If that is the policy, what is its impact on tuition pricing decisions? How have these policies differed in public versus independent institutions?
- To what extent has institutional aid served to fill in for the loss of state and federal aid in the independent sector?
- Assuming institutional aid has increased, will other key expenditures be forced to grow more slowly?
- What happens to enrollments when a surge of new aid becomes available? Are different institutions affected in different ways?

Because of its magnitude, its variability, and the reliance most institutions—particularly independent institutions—place on it, student aid is a major policy variable in the programmatic and financial shaping of California's colleges and universities. How institutions treat student aid and how government policy at both the state and federal level affects its availability make a significant difference. California's colleges and universities are certainly not neutral players in the student financial aid arena. So, in its final section, this paper attempts to explore the relationship between student financial aid and institutional finance in the various segments of higher education. Because student aid affects each segment in different ways, each will be reviewed. But the magnitude of student aid in the independent sector requires special attention be given to that sector.

1. TRENDS IN STUDENT FINANCIAL AID BY SEGMENT

Before focusing specifically on the role of student aid in institutional finance, it is important to look at the trends in financial aid over the past 12 years, on a segment by segment basis.

Chart I—Enrollments by Segment

This chart shows the 1975-76 and the 1986-87 full and part-time opening enrollments for each of the segments, except for the proprietary sector, for which data were not available. The data indicate that, in general, there has been a trend toward moderate growth in each of the segments.

While Chart I should not be used to make comparisons between the segments (due to the broad definition of part-time and the inability to estimate full-time equivalent enrollments) the chart is useful in setting context for the charts that follow, which show the distribution of financial aid among the segments.

CHART I
Opening Enrollments—Undergraduates

	1975-76	1986-87	Annual Growth Rate 1976-87
FULL TIME ONLY			
Community Colleges	374,473	261,876	(3.2%)
Cal State	170,181	188,847	1.0
U.C.	87,210	99,235	1.2
Independent	78,790	82,410	0.4
PART TIME ONLY			
Community Colleges	727,075	914,836	2.1
Cal State	68,870	73,912	0.6
U.C.	5,191	9,735	5.9
Independent	17,678	17,575	0.0
TOTAL ENROLLMENTS			
Community Colleges	1,101,548	1,176,712	0.6
Cal State	239,051	262,759	0.9
U.C.	92,401	108,988	1.5
Independent	96,468	99,985	0.3

Source: California Postsecondary Education Commission.

Chart II—California State Funds in Support of Postsecondary Education

This chart shows the total California State general funds in support of postsecondary education and the growth rates, in real terms (i.e. after inflation), by segment. Note that the overall growth was 3.3% real, per year, for the total general funds. The community colleges, the State University, and the University of California all had real growth rates that were approximately the same as the overall annual growth rate.

The chart also shows the total Cal Grant support in 1986-87 dollars and the real growth rates by segment. The independent sector was the only one to decrease in real support suffering a decline of 2.9% per year, or a total eleven year loss of 22% real. Support for the community colleges and the State University grew at over 7% real per year while support for the University of California only grew at about 2% real per year. The one sector that grew significantly was the proprietary (privately owned for-profit schools usually providing vocational education) segment, which increased at an average annual growth rate of 20% in real dollars. The total real growth in the proprietary sector over the time period was 625%.

The proprietary segment's percentage of the total has grown from 1.5% in 1975-76 to 10% in 1986-87. During that same time period, the independent sector's share dropped from 71% to less than 50%.

CHART II

California State Funds in Support of Postsecondary Education
General Fund and Cal Grant Award Amounts
(1986-87 Constant Dollars in Thousands)

GENERAL FUNDS (Excluding Cal Grant)

				Annual Growth Rate		
	1975-76	1980-81	1985-86	1976-81	1981-86	1976-86
Community Colleges	$ 879,213	$1,453,289	$1,226,512	10.6%	-3.3%	3.4%
California State University	1,141,789	1,265,270	1,561,527	2.1	4.3	3.2
University of California	1,242,538	1,428,114	1,707,457	2.8	3.6	3.2
Independent Colleges	0	0	0	0.0	0.0	0.0
Proprietary and Other Institutions	0	0	0	0.0	0.0	0.0
All Segments	$3,263,540	$4,146,674	$4,495,496	4.9%	1.6%	3.3%

CAL GRANT PROGRAM

				Annual Growth Rate		
	1975-76	1980-81	1985-86	1976-81	1981-86	1976-86
Community Colleges	$ 6,221	$ 12,207	$ 12,126	14.4%	-0.1%	6.9%
California State University	7,384	14,055	15,546	13.7	2.0	7.7
University of California	19,167	20,384	22,766	1.2	2.2	1.7
Independent Colleges	85,649	75,656	63,768	-2.5	-3.4	-2.9
Proprietary and Other Institutions	1,829	5,608	11,424	25.1	15.3	20.1
All Segments	$120,249	$127,910	$125,629	1.2%	-0.4%	0.4%

Source: California Student Aid Commission. California CPI used to calculate constant dollars.

Chart III—Non-GSL Federal Student Aid in California—Summary

This chart shows a summary of the non-GSL federal financial aid in 1986-87 dollars and the growth rates by segment. Note that the totals have remained relatively constant in real terms with the only major changes coming in the community colleges which are down 3.6% per year and the proprietaries which grew by 8.2% real per year. These significant growth rates in recent years now means that the proprietary institutions receive more non-GSL federal aid than any other segment of post-secondary education in California.

CHART III

Non-GSL Federal Student Aid in California Segments
Pell Grants, SEOG, Perkins Loans, and College Work Study
(1986-87 Constant Dollars in Thousands)

				Annual Growth Rate		
	1975-76	1980-81	1985-86	1976-81	1981-86	1976-86
Community Colleges	$140,910	$108,103	$97,964	-5.2%	-2.0%	-3.6%
California State University	70,221	68,963	77,796	-0.4	2.4	1.0
University of California	51,008	53,356	52,415	0.9	-0.4	0.3
Independent Colleges	60,471	78,460	63,291	5.3	-4.2	0.5
Proprietary and Other Institutions	50,643	62,748	111,114	4.4	12.1	8.2
All Segments	$373,253	$371,630	$402,579	-0.1%	1.6%	0.8%

Source: California Student Aid Commission. California CPI used to calculate constant dollars.

Chart IV—Non-GSL Federal Funding by Segment and by Type of Aid—Detail by Program

Chart IV breaks Chart III down by sources of funding. It shows that all the growth in non-GSL federal aid has come in the Major Grant Program category (Pell and SEOG), which has grown at an annual real rate of 4% per year. The two other categories, Perkins Loans (formerly the National Direct Student Loan Program) and College Work Study have dropped almost 12% and 4% per year, respectively.

CHART IV

Non-GSL Federal Student Aid in California Segments by Type of Funding

(1986-87 Constant Dollars in Thousands)

MAJOR GRANT PROGRAMS (Pell and SEOG)

	1975-76	1980-81	1985-86	Annual Growth Rate 1976-86
Community Colleges	$103,822	$ 84,241	$ 80,418	-2.5%
California State University	34,104	51,435	66,324	6.9
University of California	22,025	33,598	38,740	5.8
Independent Colleges	31,321	47,771	40,355	2.6
Proprietary and Other Institutions	31,884	50,098	104,157	12.6
All Segments	$223,156	$267,142	$329,994	4.0%

PERKINS LOANS (Capital Contribution)

	1975-76	1980-81	1985-86	Annual Growth Rate 1976-86
Community Colleges	$ 7,288	$ 4,093	$ 1,321	-15.7%
California State University	19,729	4,512	1,288	-23.9
University of California	12,923	7,316	3,434	-12.4
Independent Colleges	16,539	13,047	9,419	-5.5
Proprietary and Other Institutions	16,225	11,496	5,253	-10.7
All Segments	$72,704	$40,464	$20,714	-11.8%

COLLEGE WORK STUDY

	1975-76	1980-81	1985-86	Annual Growth Rate 1976-86
Community Colleges	$29,800	$19,769	$16,225	-5.9%
California State University	16,389	13,016	10,184	-4.6
University of California	16,060	12,442	10,241	-4.4
Independent Colleges	12,611	17,642	13,517	0.7
Proprietary and Other Institutions	2,534	1,155	1,704	-3.9
All Segments	$77,393	$64,024	$51,871	-3.9%

Source: California Student Aid Commission. California CPI used to calculate constant dollars.

Chart V—GSL Lending by Segment

Chart V includes the actual number of loans in each segment since 1980-81. It is important to note that while the number of loans has been increasing, the total dollars are about the same in real terms. This means that the average loan size is declining in real terms.

CHART V

California Guaranteed Student Loan Program
Number of Loans and Dollar Amounts by Segment
(1986-87 Constant Dollars in Thousands)

	1980-81		1985-86		Annual Growth Rate 1981-86	
	Number	Amount	Number	Amount	Number	Amount
Community Colleges	26,680	$ 73,205	28,598	$ 64,116	1.4%	-2.6%
California State University	45,776	139,907	46,185	118,361	0.2	-3.3
University of California	30,111	104,461	31,482	91,763	0.9	-2.6
Independent Colleges	50,848	205,708	56,431	187,406	2.1	-1.8
Proprietary	18,587	59,233	66,792	167,767	29.2	23.1
Other Institutions*	10,960	41,572	15,862	49,751	7.7	3.7
All Segments	182,962	$624,087	245,350	$679,164	6.0%	1.7%

Source: California Student Aid Commission. California CPI used to calculate constant dollars.
*Includes out of state.

Chart VI—All Federal Student Aid Funding in California (including GSL) by Segment.

Chart VI expands on the previous charts by including Guaranteed Student Loans (GSLs). Note that in GSLs, every segment except for the proprietaries has experienced declines in funding in the 2-3% real range. The proprietary sector, by contrast, has grown significantly—over 110% real—over this period. As noted in Chart IV, the proprietary segment receives more non-GSL Federal aid than any other segment. As this chart shows, when GSLs are added, thus producing figures for TOTAL federal aid by segment, the proprietary sector now receives more federal aid than any other postsecondary education segment in California.

CHART VI

Total Federal Student Aid in California Segments by Type of Funding
(1986-87 Constant Dollars in Thousands)

MAJOR GRANT PROGRAMS (Pell, SEOG)

	1980-81	1985-86	Annual Growth Rate 1981-86
Community Colleges	$ 84,241	$ 80,418	-0.9%
California State University	51,435	66,324	5.2
University of California	33,598	38,740	2.9
Independent	47,771	40,355	-3.3
Proprietary and Others	50,098	104,157	15.8
All Segments	$267,142	$329,994	4.3%

continued on the next page

Chart VI continued

GSL

	1980-81	1985-86	Annual Growth Rate 1981-86
Community Colleges	$ 73,205	$ 64,116	-2.6%
California State University	139,907	118,361	-3.3
University of California	104,461	91,763	-2.6
Independent	205,708	187,406	-1.8
Proprietary and Others	100,805	217,518	16.6
All Segments	$624,087	$679,164	1.7%

PERKINS LOANS (Capital Contribution)

	1980-81	1985-86	Annual Growth Rate 1981-86
Community Colleges	$ 4,093	$ 1,321	-20.2%
California State University	4,512	1,288	-22.2
University of California	7,316	3,434	-14.0
Independent	13,047	9,419	-6.3
Proprietary and Others	11,496	5,253	-14.5
All Segments	$40,464	$20,714	-12.5%

COLLEGE WORK STUDY

	1980-81	1985-86	Annual Growth Rate 1981-86
Community Colleges	$19,769	$16,225	-3.9%
California State University	13,016	10,184	-4.8
University of California	12,442	10,241	-3.8
Independent	117,642	13,517	-5.2
Proprietary and Others	1,155	1,704	8.1
All Segments	$64,024	$51,871	-4.1%

TOTAL FEDERAL STUDENT AID

	1980-81	1985-86	Annual Growth Rate 1981-86
Community Colleges	$181,308	$ 162,080	-2.2%
California State University	208,870	196,157	-1.2
University of California	157,818	144,178	-1.8
Independent	284,168	250,697	-2.5
Proprietary and Others	163,554	328,632	15.0
All Segments	$995,717	$1,081,743	1.7%

Source: California Student Aid Commission. California CPI used to calculate constant dollars.

Chart VII—Total Government Student Aid (State and Federal Combined) in California.

This chart shows total government student financial aid (state and federal combined) by segment. The accompanying pie charts show how the shares of aid have changed over the ten-year period studied.

CHART VII

Government Student Aid (State and Federal Combined) in California by Type and Segment

(1986-87 Constant Dollars in Thousands)

	1975-76	1980-81	1985-86	Annual Growth Rate 1976-86
Community Colleges				
Scholarship & Grant	$253,234	$111,169	$ 79,457	-10.9%
Loan Aid	15,960	77,328	66,970	15.4
Work Aid	20,374	19,776	12,752	-4.6
Total	$289,568	$208,273	$159,179	-5.8%
CSU				
Scholarship & Grant	$ 48,474	$ 76,139	$107,681	8.3%
Loan Aid	62,324	158,144	130,236	7.6
Work Aid	21,189	11,722	8,879	-8.3
Total	$131,987	$246,006	$246,796	6.5%
UC				
Scholarship & Grant	$ 65,497	$ 71,182	$ 73,274	1.1%
Loan Aid	52,065	142,184	111,741	7.9
Work Aid	15,860	11,377	10,267	-4.2
Total	$133,422	$224,742	$195,282	3.9%
Independent				
Scholarship & Grant	$165,064	$127,123	$ 98,932	-5%
Loan Aid	80,436	218,839	206,945	10
Work Aid	7,004	17,649	14,353	7.4
Total	$252,504	$363,611	$320,230	2.4%
Proprietary and Others				
Scholarship & Grant	$33,713	$ 55,535	$115,581	13.1%
Loan Aid	16,225	71,661	175,419	26.9
Work Aid	2,534	1,155	1,704	-3.9
Total	$52,472	$128,351	$292,704	18.8%
All Segments				
Scholarship & Grant	$565,981	$ 441,147	$ 474,926	-1.7%
Loan Aid	227,010	668,156	691,311	11.8
Work Aid	66,961	61,680	47,955	-3.3
GRAND TOTAL	$859,953	$1,170,983	$1,214,192	3.5%

Source: California Student Aid Commission. California CPI used to calculate constant dollars.

Shares of Total Government Student Aid by Segment in California

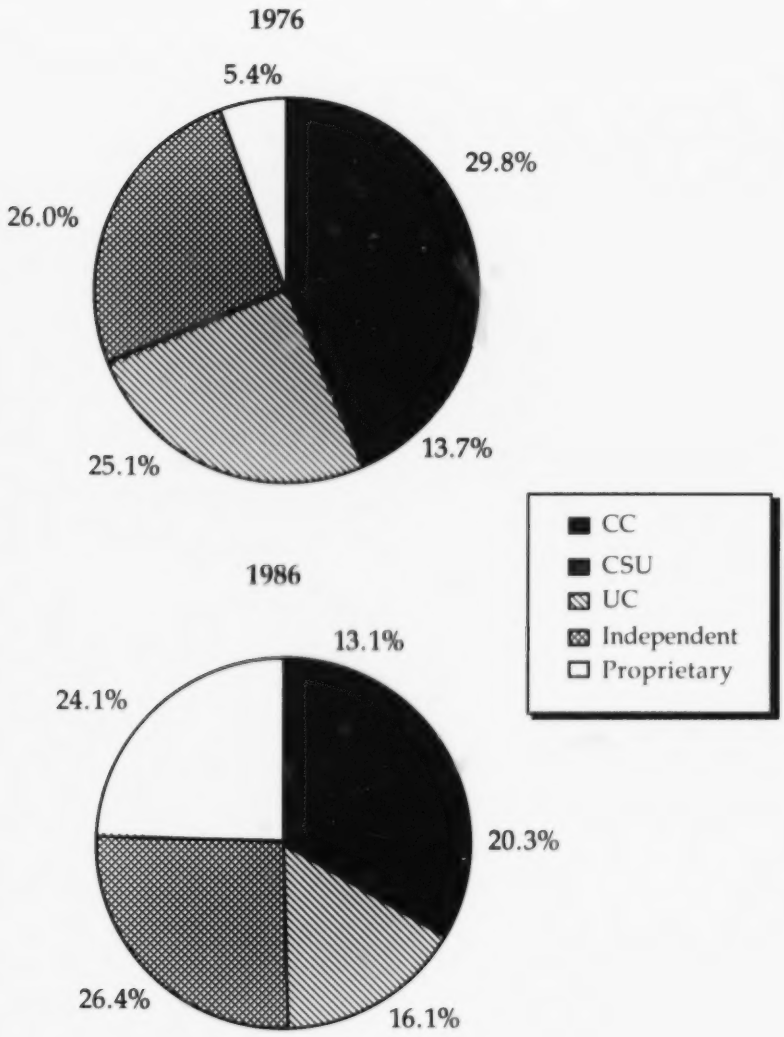

Chart VIII—Total Student Aid by Type and Segment.

This chart shows a ten year review of total (all government and institutional) student aid by segment.

Note that the loan component has grown significantly in the 80s. In constant dollar terms loans in 1985-86 were 47% of total student aid, whereas ten years earlier they were about 24%. This phenomenon has been true elsewhere in the country.

Although it may simplify the situation somewhat, this dramatic growth in loans occurred in California because of three factors—the creation of the California Guaranteed Student Loan program which helped to bring the banks back into the GSL program, the full implementation of the Middle Income Student Assistance Act and the increased availability of loans it created, and the failure of government scholarship and grant programs to keep up with inflation and tuition growth in many of the segments.

CHART VIII

Total Student Aid from Government and Institutional Sources in California by Type and Segment

(1986-87 Constant Dollars in Thousands)

	1975-76		1980-81		1985-86		Annual Growth Rate 1976-86
Community Colleges							
Scholarship & Grants	$253,234	82.6%	$113,784	52.2%	$ 83,709	45.6%	-10.5%
Loan Aid	17,191	5.6	77,753	35.6	68,090	37.1	14.8
Work Aid	36,334	11.8	$26,572	12.2	$31,740	17.3	-1.3
Total	$306,759	100.0%	$218,109	100.0%	$183,540	100.0%	-5.0%
CSU							
Scholarship & Grants	$ 48,474	36.0%	$ 82,231	30.4%	$122,040	43.6%	9.7%
Loan Aid	62,324	46.3	160,097	59.2	131,771	47.1	7.8
Work Aid	23,755	17.7	28,250	10.4	25,874	9.3	0.9
Total	$134,553	100.0%	$270,579	100.0%	$279,684	100.0%	7.6%
UC							
Scholarship & Grants	$138,305	60.2%	$137,924	44.6%	$153,498	52.6%	1.0%
Loan Aid	69,088	30.1	154,277	49.9	125,675	43.0	6.2
Work Aid	22,233	9.7	17,074	5.5	12,860	4.4	-5.3
Total	$229,627	100.0%	$309,275	100.0%	$292,033	100.0%	2.4%
Independent							
Scholarship & Grants	$237,011	68.5%	$175,148	40.6%	$226,181	47.5%	-0.5%
Loan Aid	89,987	26.0	229,615	53.2	219,611	46.1	9.3
Work Aid	19,101	5.5	26,814	6.2	30,391	6.4	4.8
Total	$346,098	100.0%	$431,577	100.0%	$476,182	100.0%	3.2%
Proprietary and Others							
Scholarship & Grants	$33,713	61.4%	$ 55,513	42.8%	$115,581	39.4%	13.1%
Loan Aid	18,027	328	72,858	56.1	176,002	59.9	25.6
Work Aid	3,169	5.8	1,443	1.1	2,130	0.7	-3.9
Total	$54,909	100.0%	$129,815	100.0%	$293,714	100.0%	18.3%
All Segments							
Scholarship & Grants	$ 710,737	66.3%	$ 564,601	41.5%	$ 701,009	46.0%	-0.1%
Loan Aid	256,617	23.9	694,601	51.1	721,149	47.3	10.9
Work Aid	104,592	9.8	100,153	7.4	102,994	6.8%	0.2%
GRAND TOTAL	$1,071,946	100.0%	$1,359,355	100.0%	$1,525,153	100.0%	3.6%

Source: California Student Aid Commission. California CPI used to calculate constant dollars.

In summary, there have been three significant changes in student financial aid funding since 1975-76:

1. the tremendous increase in government financial aid that has gone to the proprietary sector,
2. the shift in funding from scholarships to loans, and
3. the fact that there has been a decline—or no real growth—in government student aid in all segments of California postsecondary education, except for the proprietary institutions.

2. STUDENT FINANCIAL AID PROGRAMS AND THEIR IMPACTS ON INSTITUTIONAL FINANCE

I. Direct and Indirect Price Subsidies

There's a natural tendency to think of student financial aid only in terms of the direct aid offered to students. This aid takes the form of grant, loan, and job *programs*. Each of these programs is provided by governments, institutions, private individuals, or organizations. Together, they represent a direct and recognized form of assistance to students. Yet we often forget the vast amount of indirect student support that already exists in every segment of higher education in California. All along the price spectrum—from community colleges to the higher priced independent institutions—the posted price is less than the full cost of educating a student.

In the three public segments, where low fees and access have been longstanding state policy, public subsidies account for almost all of the average cost of education. So before a dollar has been spent on program-based direct student financial aid, a substantial portion of the cost of providing that education has already been paid by the state.

In independent institutions, as well, tuition does not cover the full cost of education. The absence of a direct subsidy from the state requires that tuition cover a larger portion of educational costs than in the public sector. But even in the institutions where tuition is 90% of operating income, there are usually private donations that contribute to operating revenue. And donors are encouraged by the tax laws to make such contributions. In those better endowed independent institutions, where tuition pays for a smaller share of operating expense, the subsidy to the student is even greater. Among the most highly endowed institutions in California, tuition may cover only 60% of actual educational costs. On a per student basis this may amount to an annual subsidy of $5,000-$7,000. Students on financial aid receive an even *greater* subsidy, depending on their need and on the aid policy of the institution.

The point here is simply that the concept of student aid, as defined by the various programs, does not acknowledge society's full commitment to financial support for students. Every student in California is receiving aid of some sort, even if the student is not part of any formally defined student aid program. Clearly, the subsidy is far greater in a public institution than in the private sector, but the subsidy exists there too. Although the rest of this analysis will not focus on these indirect subsidies and will instead concentrate on the traditionally defined student aid programs, it is important for the reader to keep in mind how much each institution and each student has already received from public and private support before financial aid programs are applied.

Having recognized the underlying subsidies, how do student financial aid programs affect the financial structure of the state's colleges and universities? As a point of departure, the first issue to consider is the amount of aid that's under direct control

of the institution. Who controls aid and how much flexibility exists to move money in and out of financial aid plays an important role in assessing the relationship between student aid and institutional finance. And as we'll learn, there is greater institutional control of aid funds in the independent sector than elsewhere in California postsecondary education.

With the issue of flexibility as a starting point—and to which we will return as we continue—there are two ways to gain an overview of the role of aid in institutional finance. The first is to describe in general terms the principal government student aid programs and their notable effects on institutional finance. And the second is to review comparatively the role of aid in each segment. The first analysis follows, and the second is conducted in the next chapter.

II. Government Student Aid Programs

As noted in the first report of The Eureka Project, "Origins and Outcomes—An Essay on the History of Student Financial Aid in California," annual student financial aid expenditures in California from all sources currently exceed $1.5 billion. But this vast sum is disbursed through a multitude of federal, state, and institutional programs—with differing effects on the finances of the state's higher education institutions. The following discussion attempts to review briefly the major programs at the federal and state levels—and their effects on college and university finance.

Federal Programs

Direct Payment Programs

Historically, there have been three direct payment programs at the federal level, principally for undergraduate students—the GI Bill, Social Security, and the Pell Grant program. Each of these programs was created to aid a particular group of individuals—those with military service, those with a relationship to a social security recipient, and those at the lowest income levels of society. They were not viewed as aid to higher education or as aid to the ordinary college student. (Finn, *op. cit.*, p. 74)

With support for most Vietnam era veterans winding down, and with the ending of social security dependent benefits in 1981, the only direct payment program of any significance remaining is the Pell Grant Program. To the extent there is a national college access program, the Pell Grant Program is it. *However, Pell Grants may not exceed 60%* of the student budget (including tuition/fees and room and board). Thus, access even at the lowest priced institutions is not assured. (The rule used to be 50% but was changed in 1984-85.) This 60% cost provision has the effect of making the program somewhat tuition sensitive and thereby giving students some measure of choice. For example, a student with a zero student aid index (parent and student contribution) at a community college would be eligible for $1,200. That same student with a zero index attending an independent college would be eligible for $2,100.

Institutional Impacts of Direct Payment Programs: It is important to note that the Pell program was not designed to help institutions. However, it is clear there are indirect effects at the institutional level. As Robert N. Kelly notes in "High Costs, High Need: The Independent College and Student Assistance," the Pell program "helps students in the public and independent sectors. The institutions helped least by the program are the selective higher cost independent colleges. However, even to these colleges the program is immensely valuable because it reduces considerably the need to use institutional grant money in attracting lower income students to maintain a diverse student body. In states where there are state, need based programs limited to resident, independent college students, high need students enrolling on a full time basis may have a lower net cost after grants at an independent college than at a public community college."

Perhaps Kelly's final assertion applied at one time in California, but the growing tuition gap between public and independent higher education in California means that there are no low cost independent colleges remaining. So although the Pell program does help independent colleges, it certainly does not provide an advantage to the independent sector. The growth of the tuition gap has essentially removed any advantage that might have been provided under the financial conditions of an earlier era.

As important as the Pell program is, it is not within the control of colleges and universities. One of the most obvious manifestations of this is that the Pell program has its own needs analysis system, designed by the Federal Government. The Pell needs analysis system differs from the Uniform Methodology, a system over which colleges and universities

have exercised greater influence. This complicates the program, making it less attractive to institutions than the campus-based programs—to which we now turn.

Campus-Based Programs

Funding amounts for the three campus-based programs—SEOG, College Work Study, and NDSL (Perkins)—are determined by state allotment formulas. Although the amounts may change from year to year, they are not predicated on the college admitting students on aid. Institutions apply directly to the Department of Education for campus-based funds. Under the revised 1988-89 rules institutions will receive their 1985-86 amounts as a base-year guarantee. Of the remaining funds available nationally, the first 25% will be allocated on a pro rata basis. The final 75% will be allocated on a "fair share" basis to reflect the remaining need of students at all institutions.

Institutional Impacts of Campus Based Programs: In general, the campus-based programs provide institutions with greater reliability and flexibility than under the Pell Grant program. However, on July 1, 1988 the methodology for determining need for any Title IV money will be in the hands of the Congress. It is too early to tell what the implications of a different form of needs analysis will be on institutions. It is likely there will be changes. Institutional influence over the methodology is likely to diminish, and with it the predictability that is so helpful for planning and budgeting purposes. The extent to which results will differ remains to be seen.

The Perkins Loan Program (formerly the National Direct Student Loan Program) deserves special mention here, given its impacts on the finances of those participating in the program. The principal advanatages of the program are twofold: first, the control over the loan rests with the institution, and second, the interest rate to the student is low—5% under the current program (no interest while the student is in school). The college or university can make the loan when it chooses and is not subject to the delays often experienced under the GSL program at commercial lending institutions. And, such a low interest rate can make a difference in reducing the cost of providing access.

But there is a price that institutions must pay for the control and flexibility provided under the Perkins program. To participate in the program each institution must match $1 for every $9 contributed by the Federal government. And with just a 5% interest rate charged to students, the institution is foregoing a higher return on those funds that could likely be earned in the outside market. Another cost burden is that the institution must collect its own loans—or contract that work to another party. This is an effort not every institution can afford, even with the administrative allowance provided by the government. Consequently, it can be argued that because of these administrative burdens only the wealthier institutions can afford to be in the program. While it is difficult to prove this, the data show that only $3 million of the approximately $60 million in Perkins loans in California are going to community college students. Part of the reason for this phenomenon is likely to be the administrative burden of managing this program, which many community colleges are not equipped or willing to handle—or they simply recognize that other priorities are more important.

Loans: The Guaranteed Student Loan (GSL) and the Growth of Institutional Loans

The principal national student loan program is the GSL. Every segment of postsecondary education in California relies to some degree on the GSL program. Although the growth in GSL volume has been most significant in the proprietary and independent sectors, there is strong reliance in the public sectors as well. These loans have typically been viewed as a way of providing an extra measure of funding to provide for choice, hence their clear importance to the independent colleges. In the public sector, loans have also played a role in promoting access by providing funds primarily for student living expenses. And they are certainly crucial in providing support for professional school students (business, medicine, dentistry, and law) where grant programs are essentially non-existent.

The tightened needs analysis provisions for the GSL Program included in the 1986 reauthorization legislation have begun to force some families into alternative loan programs, notably CLAS and a number of new programs created by private financial entities and educational institutions. This phenomenon had begun prior to 1986 as many students were bumping up against the annual and cumulative borrowing limits of the GSL. According to the Student Aid Commission, institutional loan programs have grown from $20 million in 1980-81 to almost $28 million in 1986-87. Families are clearly looking for new sources of loan capital, and independent colleges, in particular, have a strong interest in making it available.

State Student Incentive Grant Program (SSIG)

Many observers of student aid programs have termed SSIG the best way to integrate state and federal student aid efforts and provide an additional element of choice for students. (Finn: *Scholars, Dollars, and Bureaucrats,* p. 80) Although the program has received minimal funding from the federal government ($76 million in 1986-87), California has fared well with $12 million. The funds are used to match and extend those of the state provided for Cal Grant recipients.

From the perspective of the student and the institution, SSIG money is essentially transparent in the funding of a Cal Grant. There is no designation on the grant identifying source of funds. Moreover, the institution plays no direct role in determining how much SSIG funding flows into the state. And from the perspective of the campus administrator, there are no complex forms to fill out, as with the campus-based programs. For all intents and purposes, the institutions are bit players in the SSIG cast of characters. Essentially, the key actors are the legislature and the Governor who determine the number of grants and the maximum award. Once that is done, the Student Aid Commission simply supplements state money with SSIG in funding the legislated number of grants.

State Programs

Cal Grant Program

To help financially needy California students the State funds and operates three grant programs. The oldest of these programs, the Cal Grant A Program, assists needy students with demonstrable records of outstanding academic ability. It is the State's only scholarship program designed to meet the needs of the most academically talented. It was originally created in 1955 as the California State Scholarship Program, and was designed to enable needy and academically talented students to attend the college of their choice in California and to reduce the cost to the State of providing additional facilities by enabling more students to attend independent colleges. The Cal Grant B Program assists needy students from societal groups that have been historically underrepresented in higher education. The Cal Grant C Program assists students seeking a vocational education.

From the institutional perspective the Cal Grant program initially was a boon to the independent sector with upwards of two thirds of the Cal Grant recipients attending those colleges in the early 60s. By 1986, however, only about 30% of Cal Grant winners attended independent colleges. (See *Origins and Outcomes,* pp. 32-35 for a more complete discussion of the impact of changes in the Cal Grant program on the independent sector.) This has been due in part to the erratic growth in the level of maximum grant and the ceiling on family income and assets of eligible applicants. These ceilings had a pronounced effect in the high inflation years of the late 70s and early 80s when the maximum grant was held relatively constant while the average independent sector tuition grew significantly.

Although the Cal Grant program has not kept pace with tuition growth in the independent sector, it remains critical to those institutions. The $60 million of the total $118 million in Cal Grants going to the independent sector helps to reduce the tuition gap and certainly makes the independent sector more price competitive.

3. THE ROLE OF STUDENT FINANCIAL AID IN INSTITUTIONAL FINANCE—AN ANALYSIS BY SEGMENT

Although an overview of the major student aid programs provides one perspective on the relationship of student aid to institutional finance, one needs to look at each segment of higher education individually for a more in-depth understanding. In considering the relationship by segment our approach shall be generally descriptive but with two important foci. First, we shall pay particular attention to the relative flexibility of student aid within each segment. How much control does an institution have over its student aid and what role does aid play in relation to other important expenditures? Second, the last decade has seen considerable changes in the role of governments in student aid. So the focus here will be on the effects of these changes in each segment.

Independent Colleges

There are two fundamental reasons why the relationship between student financial aid and the finances of independent colleges is so important. The first is that financial aid serves to reduce the tuition gap between the public and independent sectors. In a state where the public sector is so large relative to the independent colleges, the price differential is a critical element to the relative attractiveness of the independent colleges. Student aid clearly plays a key role in helping the independent sector enroll students, in particular the kinds of students it wants along a whole set of academic and socio-economic criteria. In short, aid reduces the price barrier and truly expands choice.

Second, student aid in the independent sector is an important policy variable in the shaping of the institution. Unlike the public sector, where there is little control over the levels of financial aid funding at the institutional level, each independent institution can control how much of its own resources it puts into aid. This decision has effects on tuition and on other institutional priorities.

To gain a more detailed perspective on the role of aid in the finances of the independent sector, a sample of 12 independent colleges was developed for further analysis. Institutions were selected from each of the six groups established and labeled by the Association of Independent California Colleges and Universities. They included:

Group 1—Research universities—University of Southern California, Stanford
Group 2—Comprehensive universities—Loyola Marymount, Pepperdine, Santa Clara
Group 3—Endowed liberal arts colleges — Mills, Whittier
Group 4—Colleges with enrollments 800-2000—California Lutheran, Westmont
Group 5—Colleges with enrollments less than 800—California Baptist, Dominican
Group 6—Specialized institutions—San Francisco Art Institute

Based on an analysis of the sample institutions, which relied heavily on Higher Education General Information Survey (HEGIS) data, data provided directly by the institution, and on campus interviews, four general conclusions have emerged:

1. Over the past decade, there has been a vigorous institutional commitment to student aid across the independent sector. In the vast majority of the sample institutions, as government grant aid has dropped, aid from institutional sources has replaced a significant portion of it.

2. In many institutions, the commitment to institutional aid has come at the expense of mainline academic priorities, such as faculty salaries, other instructional costs, support services, and physical plant maintenance.

The severity of these impacts varies across the independent sector, but it seems to be more pronounced among the smaller less well endowed institutions.

3. The increases in institutional financial aid appear to be funded in large part out of tuition increases. Some critics have claimed that a principal cause of tuition growth in independent colleges has been increases in federal student aid. Given that our sample institutions saw their government grant aid reduced in real terms in the 1980s while loan volume was essentially flat, this criticism appears to be inaccurate in the independent sector of California.

4. The financial aid policies of many institutions appear to be in a period of change. These changes bring with them some disturbing signs about the continued ability of some independent colleges to provide a quality education to students from a variety of economic backgrounds. This can be seen in three ways. *First,* most of the sample institutions are unable to meet the full demonstrated need of their students. Leaving an unfunded gap between the student budget and the total resources available is becoming more widespread. The result is greater pressure on the student and the family to find additional funding. *Second,* the competition for students is becoming so intense that the majority of the sample schools have instituted some form of merit based scholarships. And *third,* some schools claim they are reaching the point at which their commitment to institutional aid can no longer continue. Should that happen, the potential of those institutions to maintain enrollments and achieve some level of diversity is severely jeopardized.

A discussion of these four points follows.

1. The Commitment to Student Financial Aid. The late 70s and early 80s were marked by significant declines in state and federal government support for grant aid at the sample institutions. To compensate for the loss in government support institutional expenditures exploded in constant dollar terms. Figures 1-5 show the percentage change in institutional grant aid from 1977-1986 compared to the changes in the principal government grant programs for the sample schools in each of the five groups. (A separate figure is not shown for the Group 6 institution because there was only one institution in the sample. However, the trends evident in the Group 4 and 5 schools are apparent in the single sample school from Group 6.) The results are strikingly similar across the groups of schools: significant drops in government aid have been replaced by institutional funds.

It is also instructive to understand how institutional reliance on federal student aid has changed in the decade of the 80s. By looking at a sample of three schools—one each from Groups 2,3, and 4—and taking the ratio of federal aid (Pell, SEOG, and GSL) to total tuition, room and board income, one can see how reliance on the federal government has fallen.

TABLE I

Total Federal Student Financial Aid as a Percentage of Tuition, Room and Board Income at Three Sample Independent Colleges

	1980-81	*1985-86*
Group 2 Institution	10%	6%
Group 3 Institution	24%	16%
Group 4 Institution	16%	12%

By contrast, general funded institutional aid as a percentage of tuition revenue has been increasing in the sample schools:

TABLE II

Institutional Aid Supported by General Funds as a Percentage of Tuition Income at Three Sample Independent Colleges

	1980-81	*1985-86*
Group 2 Institution	5%	6%
Group 3 Institution	10%	18%
Group 4 Institution	10%	17%

This simply confirms that the dependence on federal aid has been dropping and has been at least partially compensated for by increases in institutional funding. The question now, however, is what has been the effect of this policy on other important expenditure components of the institution?

2. Consequences of the Commitment to Student Financial Aid.

As shown in Figures 1-5, in each group of sample institutions student aid has been by far the fastest growing budget item over the past decade. Attempting to assess the impacts of this shift in funding sources is difficult without looking across the entire independent segment. But it does appear, particularly among the smaller institutions, that there have been effects on the academic program. Take, for example, the increases in instruction. Although there have been real increases in instruction in each grouping of independent colleges, most of these increases came in the latter years of the decade, compensating for the losses—or slow growth of the late 70s or early 80s. Faculty salary levels continue to be a problem in many independent colleges. They will become even more problematic as the much predicted faculty shortage becomes a reality in the 1990s and these institutions find themselves with difficulties in hiring.

The independent colleges in our sample also face other important needs, such as integrating instructional computing equipment into the curriculum, updating lab facilities, and keeping library materials current. Building in a provision for these kinds of improvements and for general support of the academic program is critical to the ability of independent colleges to perform their mission—namely to provide high quality instruction in an increasingly technological world.

But the significant commitment to financial aid has done more than just severely limit the colleges' ability to respond to new program needs. It has also eroded their ability to maintain the physical integrity of the campuses. The vast majority of the institutions in our sample expressed great concern about the growing level of facilities decay. History has shown that in times of budget stringency, maintenance is usually the first area to be cut. And restoring those cuts in maintenance while attempting to respond to the financial aid problems and the need for program improvements presents an almost overwhelming challenge, particularly in the smaller institutions.

While this paper does not attempt a detailed assessment of the financial strength of California's independent colleges and universities, it does appear that there is reason for concern. Put simply, the concern is that these institutions—particularly the smaller colleges—can no longer maintain a commitment both to socio-economic diversity and to quality education. Unfortunately, without a quality program the commitment to diversity is not productive for society, and without diversity the quality of the educational experience for those students who remain is weakened.

FIGURE 1

Growth Rates (in Real Terms) of Financial Aid Compared to Other Key Institutional Expenditures for Group 1 Schools

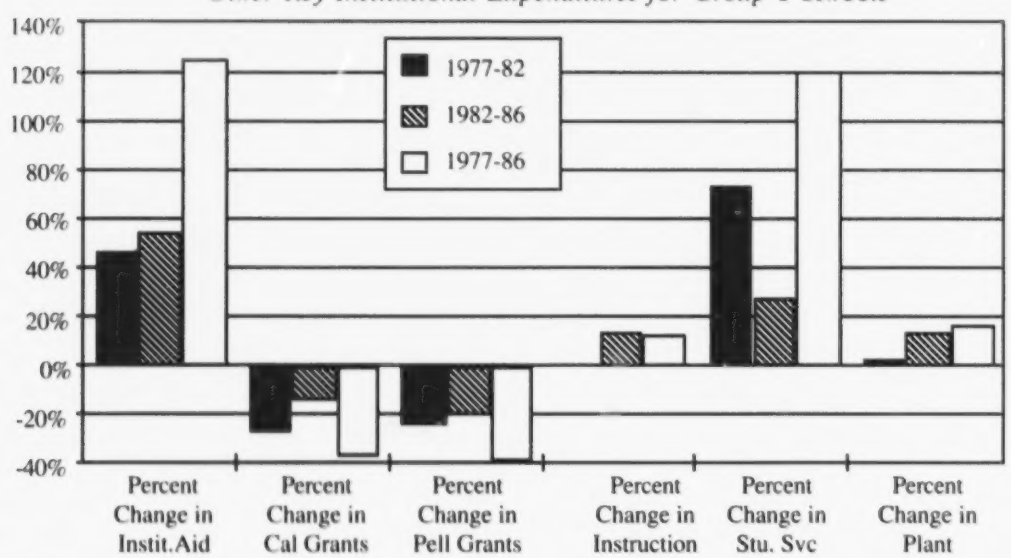

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FIGURE 2

Comparison of Growth Rates (in Real Terms) of Financial Aid and Other Key Institutional Expenditures for Group 2 Schools

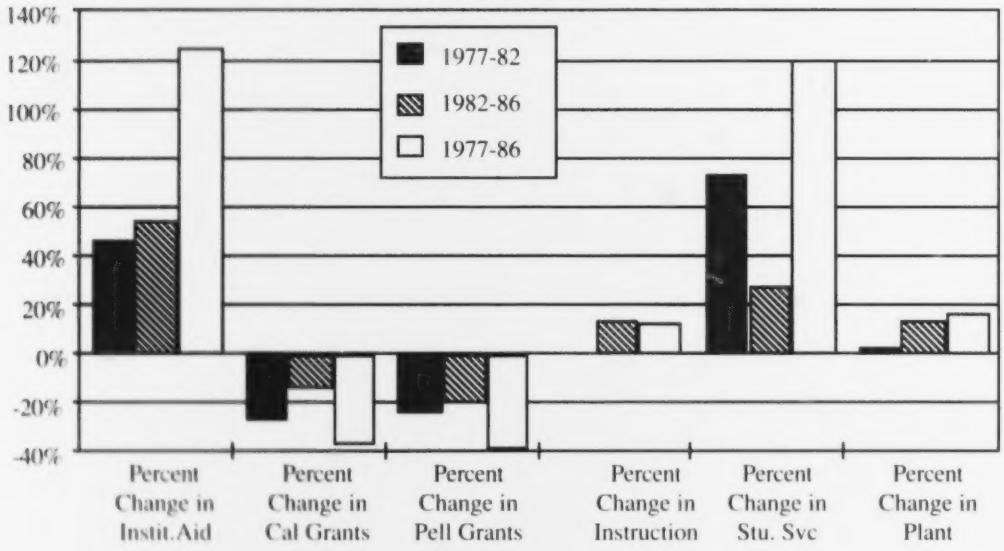

FIGURE 3

Comparison of Growth Rates (in Real Terms) of Financial Aid and Other Key Institutional Expenditures in Group 3 Schools

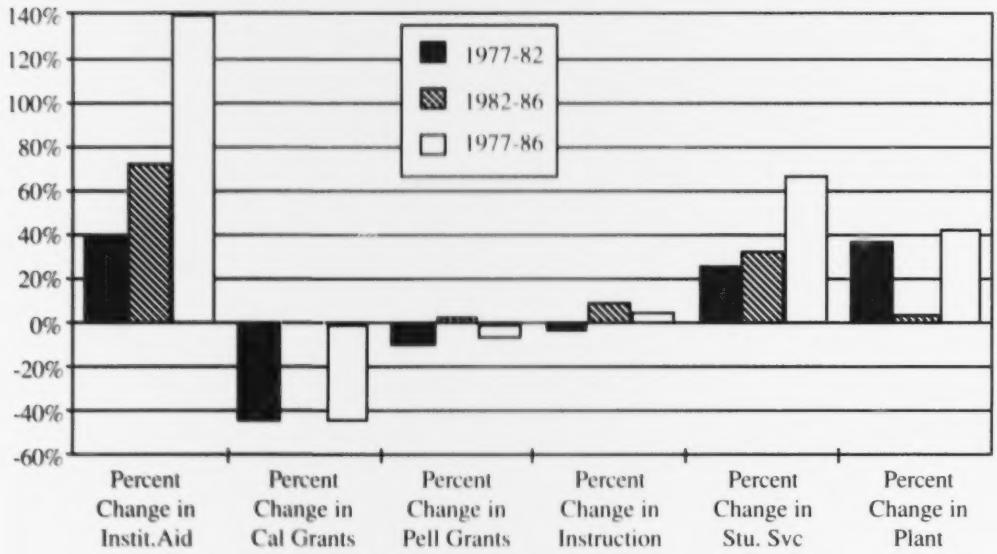

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FIGURE 4

Comparison of Growth Rates (in Real Terms) of Financial Aid and Other Key Institutional Expenditures in Group 4 Schools

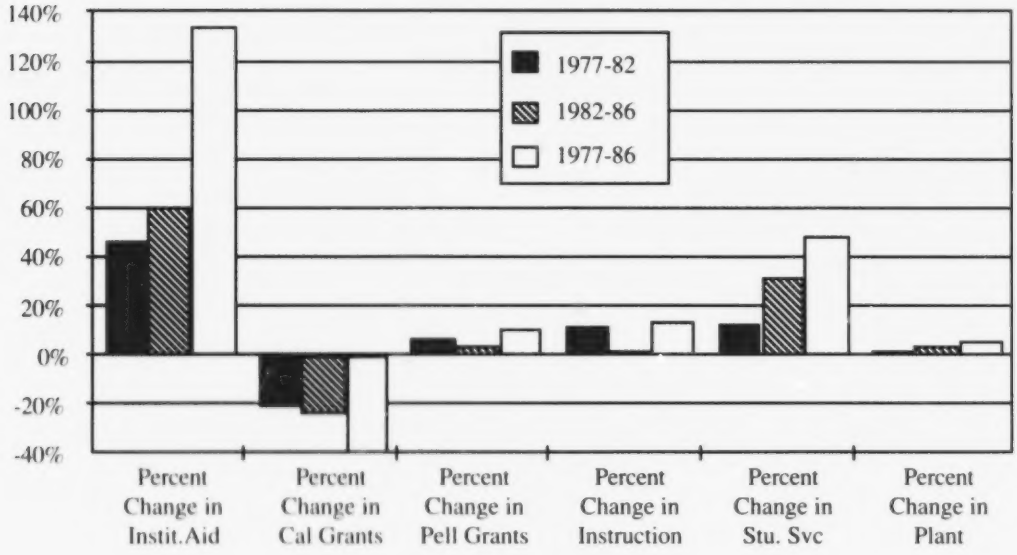
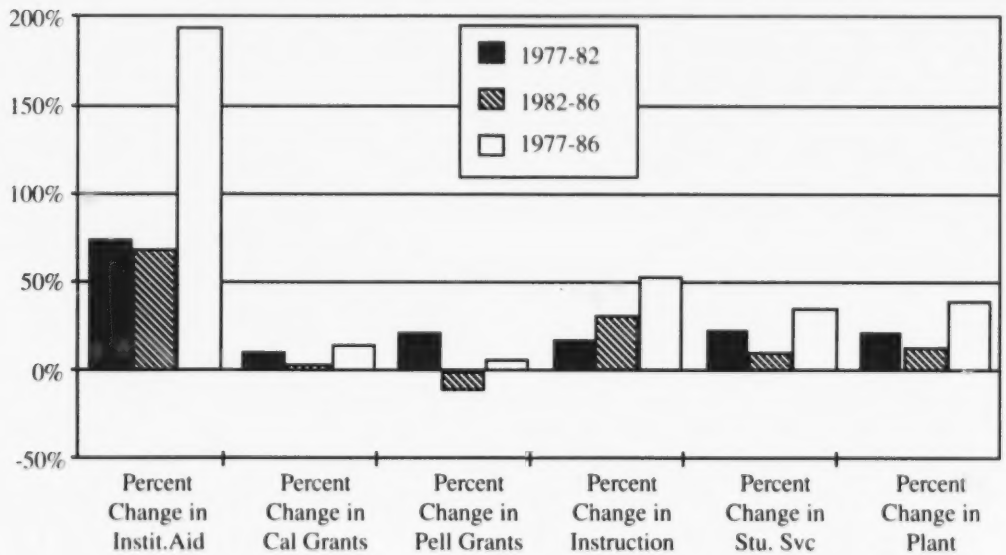


FIGURE 5

Comparison of Growth Rates (in Real Terms) of Financial Aid and Other Key Institutional Expenditures for Group 5 Schools



Data sources for Figures 1-5 are: U.S. Department of Education, California Student Aid Commission, and institutional data. GNP inflator used to calculate constant 1985-86 dollars.

3. Financing the Increases in Institutional Aid. In most of the sample institutions the increases in student aid have been paid, for the most part, by increases in tuition, by slowing the growth in other institutional expenditures from what they may otherwise have been, and by increasing restricted sources of student aid (i.e. gifts and endowments restricted to student aid). It is not surprising that tuition plays the most significant role in that regard given that it is the largest source of revenue for independent colleges, ranging from 47%-90%. (Other sources of revenue on which most institutions rely and which could be used for financial aid would include gifts, endowment income, and surpluses derived from auxiliary enterprises.)

The argument has often been made that institutions charge higher tuitions to those who can pay in order to fund their aid budgets, which then support needy students. That argument is then carried one step further stressing that institutions have asked students and their families to fund student aid. Although there is certainly some income redistribution at work here, it's important to remember that even full tuition paying families are not paying the full cost of education. And, until they do, it is plausible to argue that incremental tuition dollars are simply offsetting educational costs paid by other sources of funds.

The growth in institutional aid in the light of falling government grant funding raises questions about the assertion that increases in government aid have contributed to the growth in tuition. In fact, the exact opposite seem to be true in the 1980s. As government aid declined, tuition went up. Whether tuitions would have increased as quickly if government aid had grown is a matter of speculation. Most likely there would have been some moderation in the growth rate of tuition. It's also likely that the incremental revenue would have gone to support expenditures other than student aid. But in any event, the fact remains that in the independent sector it's difficult to connect increases in tuition with increases in government aid simply because the latter increases haven't occurred. (See Table VII in Chapter I)

4. Changes in Aid Policy. Based on conversations with campus officials, the growth in the institutional commitment to student aid has clearly put strains on many of the sample institutions. At virtually all the institutions some important priority has been deferred or downgraded in favor of sustaining the commitment to student aid. For example, at one university student aid was given the highest priority because the full financial need of all undergraduates there was not being met, and the university felt it critical that this be done. It so happened that the commitment came when government aid was on the decline. So the institution increased its own aid by 132% from 1982-83 to 1987-88. At the same time its faculty salary rankings among comparative public and private institutions dropped by three positions. At this institution there was a recognition that increasing the funding for student aid meant fewer resources for faculty salaries. Although the effects of that decision on faculty development, morale, and retention are difficult to quantify, this university will ultimately be forced to bring its salary levels up to the competition or lose their better faculty in what is becoming a very tight market.

At other institutions the commitment to aid has been founded on a desire to keep enrollments from falling. Price discounting to reduce the net price to selected students was a frequently stated policy among some of the sample institutions—particularly those that are smaller and less well endowed. A number of these institutions have excess enrollment capacity and are clearly looking at aid as a way to increase enrollments.

But regardless of how aid is being used, a number of the sample institutions, particularly the smaller places, are reaching or have already reached the point at which the heroic institutional commitments to student aid cannot continue. There is no clear pattern of response at this point, but it seems that the following kinds of choices are being considered: a reduced commitment to diversity, heavier recruitment of students who can afford to pay full tuition (especially out of state students), a movement away from the traditional 18-24 year-old market, reduced commitment to library acquisitions, a general deterioration of the physical plant due to reduced support for maintenance, and a general downsizing of some institutions themselves. The result of these practices is likely to be a weaker independent sector.

University of California

Student financial aid at the University of California is in many ways more complex than in the other public segments of higher education in California. This is due primarily to the University's role as a

research institution and to the variety of aid programs supporting graduate students that do not exist elsewhere in the state-funded institutions. In addition, the availability of some restricted funds for undergraduate aid—a source essentially unavailable at the CSU or the community colleges—must also be considered in looking at the UC student financial aid picture.

In 1985-86 University-funded financial aid awards amounted to $77.2 million for all students. About $29.6 million of this amount went toward scholarships and fellowships for undergraduate and graduate students, essentially on the basis of merit. The University Student Aid Program of $38.6 million, which provides grant, loan, and work-study aid to students on the basis of need, is the other principal component of the $77.2 million. The $77.2 million is just 4% of the total University budget of $1.9 billion.

Until 1984-85 general funded student aid was provided by student fee income. At that time the policy changed and the state began to buy out the aid provided by fees. In 1986-87 the general fund offset rose to $35.6 million or 85% of the funding for the University's major need-based aid programs. The remaining funds for University need-based aid come primary from student fee revenues. Non-need based aid comes from endowment income, alumni and donor contributions, and campus discretionary funds.

It is interesting to note that this is exactly the opposite of what is happening in the Independent sector where increases in student aid are being paid with tuition income. And the released fee income is being used for other purposes. It is worth noting that the $35.6 million in general funded aid is the only continuing piece of the UC budget that is specifically allocated by the state for a particular program. The University has the discretion to move funds among other parts of the budget, but this provision does not apply to student aid.

One of the principal student aid funding problems facing the University of California is the inability of state support to keep up with inflation increases in the non-fee portion of the student budget. Although inflation has been low in recent years, students and their families are being forced to absorb inflation increases for subsistence. They are doing this either by tightening their own family budgets or by increased borrowing.

Another important student aid problem facing the UC system is the adequacy of financial aid for graduate students in the arts and sciences. Attracting the best graduate students is a critical priority of leading research universities, and the UC's aid for graduate students has slipped behind the competition in recent years. This is a recognized problem and one the University is pursuing actively with the Legislature and the Governor.

Community Colleges

A cursory review of the institutional finances of the California Community Colleges would indicate little *direct* relationship between student financial aid and the financial structure of this large and important segment. In making this statement, "direct" is the operative word. There is indeed little direct connection. State general funded student aid is a minor portion of the total budget of the community colleges. There was virtually no direct relationship until 1984 when the community college fee was imposed. And in a no fee environment, the financial aid provided by various government programs was used solely for living expenses. Since community colleges are commuter institutions without residential facilities, financial aid did not flow back into the institution to pay for services delivered.

That direct relationship has changed somewhat with the implementation of the fee and the appropriation of student aid in the budget. The direct allocation flows into the institution and is used by aid administrators to support the needs of students.

Although the direct effects of student aid on the community college finances are minimal, there clearly are very important indirect effects. The most significant is the relationship of aid to access and the resulting implications that increased enrollments have on state-supported funding. With the availability of aid to offset community college fees and to support living expenses, one would assume that enrollments would increase and therefore increasing the ADA counts. And the higher the ADA counts, the greater the level of direct state support. Little is understood, however, about the specific relationship between student aid and enrollments in the community colleges. There have been no studies that have looked at enrollment changes caused by changes in aid.

Although the most significant effect of student aid on the finances of community colleges is in

enrollments, there are other aspects to the relationship as well. One such aspect is counseling. In all segments of California higher education financial aid counseling is critical in making sure students avail themselves of aid opportunities. Officials in community college districts interviewed for this report consider their counseling support inadequate to meet the task.

Community college executives have some flexibility in moving funds around in their budgets to support student aid, although little movement has in fact occurred. One way, however, that student aid funds have been augmented in the community colleges has been the creation of local foundations. Although an analysis of the role of these foundations is not within the scope of this paper, they do play a growing role in supporting student aid, as well as other expenditures.

California State University

The relationship between student aid and the institutional finances at the CSU is comparable in some ways to the UC system. However, because CSU is primarily an undergraduate institution, and grant support for graduate students is almost nonexistent, there is less complexity to the relationship than at UC. As the trend analysis in Chapter I indicates, there is heavy reliance on the Federal programs and on the Cal Grant programs to provide aid to approximately 89,000 students. In addition to these standard programs, there are other programs more specific to the CSU—the Educational Opportunity Grant Program, the State University Grant Program, and the local campus restricted funds.

How do these various programs relate to the finances of the CSU? There are three important aspects of that relationship.

The first is the issue of control. Who controls the student aid funds and how much flexibility exists to move aid funds around to cover other priorities? Or, for that matter, how much flexibility exists to move non-aid funds into student aid? The short answer is "not much." Student aid at CSU is essentially a self contained enterprise. Once legislative directions have been set there is essentially no flexibility over the movement of student aid funds either system-wide or at the individual campus. Campus presidents do not have authority to reallocate student aid money to other expenditure categories, nor do they trim other expenditures to fund student aid.

A second aspect to the relationship can be found in the role financial aid plays in promoting access to a CSU education. Because the funding for CSU is allocated on a formula based on the number of students, the availability of financial aid has some impact on the number of students enrolled—and thereby on the flow of funds to the campuses.

A third aspect is the relationship between fee growth and student aid. As fees have increased in the 80s state funded student aid has increased as well. However, there is still considerable unfunded financial need in the system, since there has been no provision of state support to keep up with inflation increases in the non-fee portion of the student budget. Thus, students and their families have been forced to absorb inflation increases for subsistence by either tightening their own family budgets or by increased borrowing.

Proprietary Schools

Assessing the relationship of student financial aid to the institutional finances of the proprietary institutions has been a particularly difficult aspect of this study. The Proprietary sector is a large and diverse one with 331 institutions participating in the California GSL program. Segment-wide enrollment trends and financial information are generally unavailable in any meaningful long-term comparative manner. Perhaps the best data on financial aid in the Proprietary sector were shown in Chapter I of this report. In real dollars from 1976-1986 Proprietary sector student aid from all sources has grown by tenfold. The Proprietary sector now receives more Federal student aid than any other sector of postsecondary education in California.

Because of the lack of data, the diversity of institutions in the segment, and the significant effort in time and resources it would require, it has been beyond the scope of this study to delve further into the relationship of student aid to the finances of the institutions of the Proprietary sector. Given the dearth of understanding of the relationship, however, it is one that cries out for further study, particularly in light of the substantial commitment of Federal and State resources to students who attend Proprietary institutions.

Conclusion

Student aid is a mainstay in the financial fabric of all of California's postsecondary institutions. Each segment, regardless of its prices or its governance, is dependent to some degree—directly or indirectly—on student aid.

As this paper has attempted to demonstrate, the segment in which the connection between student aid and institutional finance seems most direct—and perhaps most fragile—is in the independent sector. Over the past decade, institutional grant aid has replaced falling support from federal and state sources. And it appears this increase in institutional aid has come at the expense of other academic priorities. This seems particularly true in the less prestigious institutions. The continued growth in grant aid in those institutions raises the question of whether they can sustain such a commitment to financial aid without further reductions in program quality. The answer is that they probably cannot.

The Introduction noted the dearth of current research on the relationship between student aid and institutional finance. Although this paper has attempted to expand the understanding of that relationship, it has said little about the role of financial aid in the proprietary sector of California. Although it was beyond the scope of the study to explore that relationship, it nevertheless needs to be done in future research. As noted in Chapter 1, the use of government student aid in proprietary institutions has grown dramatically in the past decade. Yet little is known about the connection between student aid and the financing of those institutions.

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